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No. 14

In the Supreme Court of the United States

OCTOBER TERM, 1930

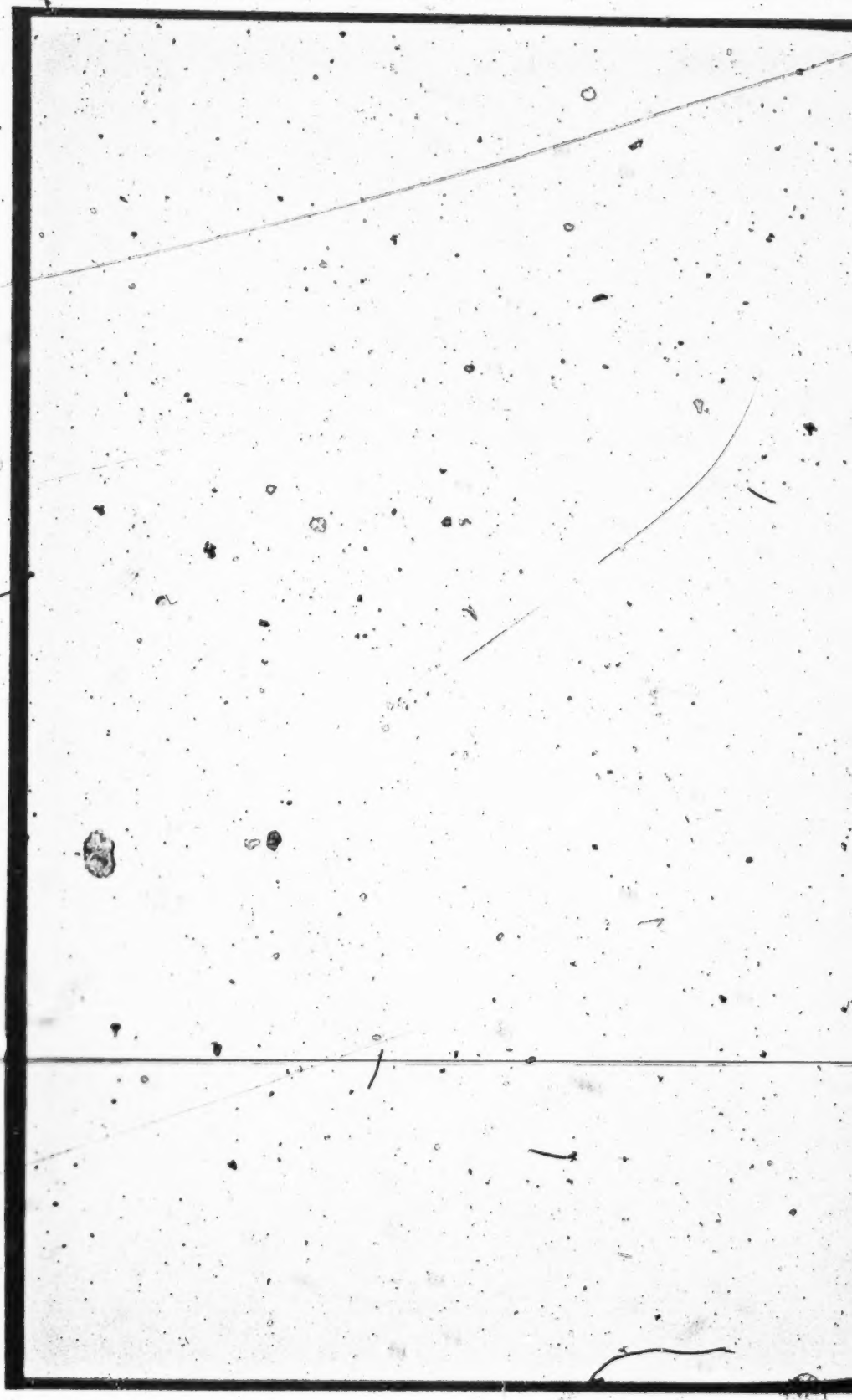
HANDY AND HARMAN, PETITIONER

v.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION



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In the Supreme Court of the United States

OCTOBER TERM, 1930

No. 709

HANDY AND HARMAN, PETITIONER

v.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 26–36) is reported in 17 B. T. A. 980. The opinion of the Circuit Court of Appeals (R. 75–79) has not been reported.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered January 12, 1931. (R. 79.) The petition for certiorari was filed February 5, 1931. The jurisdiction of this Court is invoked under Section

240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether two companies may file a consolidated income-tax return as affiliated corporations, under the Revenue Act of 1918, if the two companies are operating as a business unit and their stock is actually controlled by the same interests, even though the control is not legally enforceable.

STATUTE INVOLVED

Revenue Act of 1918, c. 18, 40 Stat. 1057, 1081:

> SEC. 240. (a) That corporations which are affiliated within the meaning of this section shall, under regulations to be prescribed by the Commissioner with the approval of the Secretary, make a consolidated return of net income and invested capital for the purposes of this title and Title III, and the taxes thereunder shall be computed and determined upon the basis of such return: * * *
>
> (b) For the purpose of this section two or more domestic corporations shall be deemed to be affiliated, * * * (2) if substantially all the stock of two or more corporations is owned or controlled by the same interests.

STATEMENT

The following findings of fact were made by the Board of Tax Appeals (R. 26–33):

Petitioner was a New York corporation, dealing in silver, and engaging in allied activities. (R. 27.) Hamilton and De Loss, Inc., a Connecticut corporation, was organized in 1916 to do the metal stamping for petitioner. (R. 28–29.) Harold H. Hamilton, an expert in the silversmithing business, was chosen president of Hamilton and De Loss, Inc. Six men owned about 94 per cent. of the stock of petitioner. (R. 29.) They also owned about 77 per cent of the stock of Hamilton and DeLoss, Inc., but in different proportions. Hamilton did not own any stock in petitioner but he was to have 20 per cent of the stock of Hamilton and De Loss, Inc., (R. 29–30.) Hamilton did not have the money to pay for the stock, and so Harry H. De Loss, vice president of both petitioner and of Hamilton and De Loss, Inc., and one of the six men mentioned above, arranged a loan to Hamilton, whereby Hamilton paid for the stock and assigned it to De Loss, the latter depositing it as collateral security for the loan. (R. 30.) Hamilton received a salary from Hamilton & De Loss. He attended all stockholders' meetings of Hamilton and De Loss, and voted his stock, but never voted in opposition to the six men owning stock in both companies. (R. 30.)

Hamilton became insolvent in 1919, and on February 1, 1919, DeLoss paid the loan and took over Hamilton's stock. (R. 30.)

Petitioner and Hamilton and DeLoss, Inc., originally filed separate returns for 1918, but subse-

quently filed a consolidated return for that year which was accepted. (R. 33.) In 1924, the then Commissioner of Internal Revenue reversed the ruling of his predecessor in office, and held that the companies were not affiliated, and assessed deficiencies in tax against petitioner of $25,800.99 for 1918. (R. 33.) The Board of Tax Appeals affirmed the ruling. (R. 38.) The Circuit Court of Appeals for the Second Circuit affirmed the judgment of the Board of Tax Appeals. (R. 79.)

The question of affiliation of the two companies after February 1, 1919, when DeLoss took over Hamilton's stock, is not involved.

ARGUMENT

The court below held there was no control within the meaning of the statute, since DeLoss could not legally enforce his control over Hamilton, although an actual control was exerted over Hamilton's stock. (R. 78.) This followed the previous decisions of the same court in *Ice Service Co.* v. *Commissioner*, 30 F. (2d) 230, and *Commissioner* v. *Adolph Hirsch and Co.*, 30 F. (2d) 645. A similar position has been taken by the Circuit Court of Appeals for the Sixth Circuit in *United States* v. *Cleveland, P. and E. R. Co., Inc.*, 42 F. (2d) 413; by the Court of Appeals of the District of Columbia in *American Auto Trimming Co.* v. *Lucas*, 37 F. (2d) 801; and by the Court of Claims in *Wadhams and Co.* v. *United States*, 67 C. Cls. 235.

The legislative history of the Revenue Acts shows, as Judge Mack pointed out in *United States v. Cleveland, P. and E. R. Co.*, *supra*, that the control intended was one legally enforceable. The 1918 Act partially incorporated Article 77 of Treasury Department Regulations 41, promulgated under the War Revenue Act of 1917, c. 63, 40 Stat. 300. The part of Article 77 not enacted related to affiliation on the basis of a business or economic unit. This part was in the bill as it left the Senate. 65th Cong., 3d Sess., H. R. 12863, Senate Calendar No. 563. But it was stricken out in conference. H. R. Conference Report No. 1037, 65th Cong., 3d Sess., p. 15, to accompany H. R. 12863. And as changed it became law.

But the Circuit Court of Appeals for the Ninth Circuit has definitely rejected the proposition that the control necessary for affiliation must be legally enforceable. *Burnet v. Wilshire Oil Co., Inc.*, decided February 9, 1931, not yet reported. Other cases adopting the same view, and holding that a control, based upon proxies, acquiescence, contracts or similar relations, was sufficient, are *Kile and Morgan Co. v. Commissioner*, 41 F. (2d) 925 (C. C. A. 1st); *J. Rogers Flannery and Co. v. Commissioner*, 42 F. (2d) 11 (C. C. A. 3rd); *Pelican Ice Co. v. Commissioner*, 37 F. (2d) 285 (C. C. A. 5th); *Great Lakes Hotel Co. v. Commissioner*, 30 F. (2d) [illegible] (C. C. A. 7th); and *Eby Shoe Co., Inc., v. United States*, 44 F. (2d) 278 (C. Cls.).

This Court had the same conflict before it in the petition of *Burnet* v. *J. Rogers Flannery and Company*, and related petitions, Nos. 523–525, October Term, 1930, but it denied certiorari December 1, 1930. Those cases held that legally enforceable control was not essential for affiliation.

The 1924 and subsequent Acts have omitted the word "control," as applied to affiliated companies, and have definitely stated that 95 per cent of the stock shall be owned by the same interests. Likewise, where the 1921 and previous Acts require ownership or control of a substantial amount of the stock of one company by another, the 1924 and subsequent Acts have struck out the word "control," and required that 95 per cent of the stock be owned in order to file a consolidated return. Revenue Act of 1924, c. 234, sec. 240, 43 Stat. 288; Revenue Act of 1926, c. 27, sec. 240, 44 Stat. 46; Revenue Act of 1928, c. 852, sec. 501 (a), 45 Stat. 869. The question in the present case can not arise under the 1924 and subsequent Acts, and so it will gradually cease to be a point of practical controversy.

Some question may remain as to what are "the same interests" under the 1924 and subsequent Acts, but the changes in the later Acts have done away with the principal sources of contention of the 1921 and earlier Acts.

A large number of cases involving consolidated returns under the Revenue Acts of 1917, 1918, and 1921 are still under consideration in the Bureau of

Internal Revenue, and although it is not practicably possible to ascertain how many cases are pending which involve the question raised in the instant case, we are not in a position to state that it may not be involved in a considerable number.

CONCLUSION

In spite of the fact that there is conflict between the decision of the court below and several other Circuit Courts of Appeals, we submit that the same reasons exist for denying the petition for certiorari which prompted the Court to deny the petition in *Burnet* v. *J. Rogers Flannery and Company* and related petitions, Nos. 523–525, October Term, 1930.

THOMAS D. THACHER,
Solicitor General.
G. A. YOUNGQUIST,
Assistant Attorney General.
CLAUDE R. BRANCH,
SEWALL KEY,
JOHN H. MCEVERS,
Special Assistants to the Attorney General,
WILLIAM H. RILEY, JR.,
Attorney.

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